Mike Green: Passive Investing Dynamics, Inflation vs. Hyperinflation, Digital Currencies & more

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Erik: Joining me now is Mike Green, Chief Strategist and portfolio manager for Logica Funds. Mike, it's great to get you on the show this one is overdue, you've really gotten a lot of popularity lately since you came out from hiding behind the compliance wall that you used to hide behind.

Let's start with a topic that I know you've touched on recently on another podcast you did with our good friends Grant Williams and Bill Fleckenstein. They did a series called the Stock Market End Game or I guess it was just called the End Game and it was fascinating to me to listen to because I used to say the exact same thing almost that Bill said in that series, which is, hey, look, this whole stock market rally since 2009 it's been artificially propelled by monetary policy, not by economic fundamentals. It's artificial and therefore it has to end badly someday, there has to be eventually a crash of the stock market or something because there's no free lunch in finance, that's just not how it works. I've changed my view, I don't really think that's true anymore, I think that it has to end badly but it's not necessarily nominal down in the stock market.

Now, you've done a bunch of research that I think is maybe a little different. I was thinking on the MMT lines of why maybe we just end up seeing more money printing and more inflation and asset prices going up not down in nominal terms, you've got maybe a different explanation for why we might see that upside.

So, first of all, do you think I'm right to consider that maybe the stock market doesn't really have to crash ever after all just because of this so-called artificial stimulus? And how did you see it? What are the drivers? Let's review some of the research that you've done on active passive.

Mike: So, I definitely think that you are both actually hitting on a key point, which is that the market is "unhealthy", right? So, the behavior that we're seeing most of us who have been involved with markets for an extended period of time can rationally look at it and say something is off and a lot of people put it at the feet of the Fed.

My analysis suggests that in more important forces actually the change in market structure driven by the growth of passive investing and in just really simple terms, the introduction of passive investing changes the character and the behavior of market participants moving it from a discretionary purchase decision where cash is a legitimate asset that can be held when valuations or economic fundamentals suggest that investing in securities would be unattractive.

When you move to a passive framework it becomes rules literally as simple as: Did you give me cash? If so then buy; and in reverse, did you ask for cash? If so then sell, with no consideration for the underlying fundamentals or the economic backdrop in which the events are occurring. That change and the reduction in cash that those funds hold versus traditional vehicles in our analysis is actually responsible for the vast majority of the price increase that we've seen relative to the fundamentals. Absolutely, there was an improvement after 2009 as the global financial crisis came to an end that supported recovery in asset prices and certainly activities like corporate share buybacks have contributed as others have noted. But by far the dominant feature appears to be this dynamic of passive investing.

And as a result, I tend to think that we need to consider both, I think it would be silly to say that markets can't crash roughly five months after they just did, right? But I also think that it's very difficult to argue that until those dynamics change, until the flow of money into passive changes, that we're going to see a significant change in the character of this behavior and I do think there's a very real risk that we break markets by having them go too high.

Erik: Let's talk a little more about what you just said. You said the mechanics here are there's no thought to economics, it's basically investors give asset managers money if so buy, if investors took money away from asset managers then sell. Well, the second half of that I think if we go back to Bill Fleckenstein's logic is, okay, that means at some point, you get a self-reinforcing vicious cycle of withdrawals where investors are taking money away from asset managers, a driver of that might be something like demographics around aging baby boomers leading to the beginning of something that develops into a self-reinforcing vicious cycle. So, does there have to be a bad ending for the stock market when eventually that process reverses? And what you're seeing is investors taking money away from asset managers, is somehow changes something in the world and passive is no longer the thing anymore?

Mike: Well, first, I think it's very difficult to have passive no longer be the thing because I think the arguments for it and the regulatory advantage that have been conferred on it are so extraordinary at the stage that we're probably going to see this to its logical conclusion. So, in really simple terms, most people think about passive in terms of an aggregate share where it's somewhere between most would say somewhere between 40 and 45% of the total market, we think it's about 44% right now. If you look at those characteristics and split them by demographics, for those in the younger generation the vast majority of their exposure in excess of 90 plus percent of their exposure to markets as we know them is through passive products. For those in the older generation it's much closer to 20% and so the dynamics in terms of passive penetration suggests that we're going to move increasingly rapidly to a world that looks more and more passive. And under that type of framework, the models that I have suggested that you should largely expect to see an inflationary condition, not inflation in terms of consumer prices but inflation in terms of the price that people will be willing to pay and the prices that we'll see in securities markets.

On the other side of that equation though is when that is happening effectively you can be thinking about the velocity or the volatility of those events is accelerating. So, I've used the analogy, it's like trying to explain to people that the brakes are broken in a car that is traveling uphill, it's actually somewhat irrelevant until you start to hit downhill, and then you hit a moment of panic. And you're fine as long as the road turns back up at some point but if you've crested the mountain and come down the other side and you have no brakes, it becomes a very scary situation.

We saw something like that I would argue in March, right? That characteristic that there's no absolute level that you can point to and say it has to turn down from here, when you're talking about this type of dynamic of moving from a population set that holds the majority of the assets that are roughly 20% passive, to a population set that will slowly accumulate those assets through contributions to 401K's, requests, etc. That doesn't necessarily have to turn down but the dynamics of gravity or the dynamics of how markets are structured suggests that at some point, it's actually likely to. Now, the simple example for that would be those who are buying in and contributing are doing so in a somewhat linear fashion, their contributions are tied to their incomes.

On the other side of the equation, those who are making withdrawals whether it's because they're hitting retirement age demographics, as you suggest, they are typically taking a fraction or a percentage of their profit or percentage of their securities out, when they do that it means that ultimately you have an increasing mismatch between the contributions coming in from incomes and the withdrawals that are coming out from withdrawals. And that would suggest that there will be a topping point that's going to happen now. That of course has happened in the past and actually that's very much what happened in 2002 when you saw the stock market crash over the summer of 2002 into July, August, September.

In response to that we have repeatedly seen central banks or policymakers step in to create substantive changes, whether that is inflating the value of bonds by cutting interest rates, directly purchasing securities as we've seen in other geographies, changing the 401K rules so that contributions can be delayed for a longer period of time, or they can be increased or to create tax incentives for employers to increase their contributions and thereby raise the quantity of money that is going in. Those are all actions that I think that we should anticipate. Ultimately, it's a question of, will you be aggressive enough to stop it and will you permanently break the markets at some point? To me that's unknowable so we remain agnostic, the trading positions we take at Logica is effectively we buy straddles, we want to participate in both directions.

Erik: Listeners, I'm going to take a quick break here. I wanted to start with this topic of the influence of passive investing on the market give you a little bit of a teaser of that because Mike's work in this space is obviously really, really groundbreaking. I think we've got a couple of resources for you to go further on this. The first is a slide deck you'll find linked in your Research Roundup email, which gives a bunch of graphs and charts supporting this discussion of the influence of the transition from active to passive investing.

Now, we could easily spend the rest of today's interview entirely on that topic, the thing is our good friend Grant Williams did such a fantastic job of that on a podcast that's already been recorded. I'd really like to get to new ground with Mike in today's podcast, we're going to just go ahead and give you a link to Grant Williams podcast along with Bill Fleckenstein interviewing in much greater detail Mike on this subject of the transition from active to passive and its systemic and reflexive impacts on the market. It's really fascinating stuff, I recommend that you download the chart deck from the Macro Voices Research Roundup have that in front of you when you listen to Mike's interview with Grant and Bill, let's move on Mike to a few other topics.

Now, you think about this whole stock market, where is it headed? What's the ultimate end game? In terms of the passive trend a lot of people, and I'm not sure if they're right or wrong, I've definitely kind of gotten on board with this myself lately, have felt like look since 2009 ever since quantitative easing has been the thing, it seems like the stock market can only go up. So, there's some transmission mechanism, although people seem to disagree on the extent to which it exists. How much of it is just expectation versus reality? Somehow, it seems like when the Fed expands its balance sheet, the money all ends up in the stock market and a lot of people are thinking that with the rapidly growing political popularity of MMT that probably that trend is set to continue. How do you see this? Are the people who think QE drives the stock market right? Are they wrong? If so, in either direction, why? And what about MMT? How does that change the game?

Mike: Well, so in simple terms, there's nobody who's right or wrong until history tells us what's the right answer. So, we have our view on that, there is obviously an impact from QE, there is a when the Fed goes out and expands its balance sheet in particular if it is using the expansion of that balance sheet to purchase assets from the private sector. It's doing two things, one is it's raising the price of those assets because they become protected to the downside effectively or abrogating the left tail, you're also in some situations forcing people to find alternate uses of that capital.

So if I buy a corporate bond from a hedge fund they now have cash that they have to deploy and potentially have more cash than it was marked on their book or the way they were treating it, if they had had to sell it to third party into an illiquid market, right? So those dynamics, absolutely create stimulus and absolutely support asset prices. The question is, does that actually flow through in any meaningful way into economic activity? And we're not seeing any meaningful evidence of that.

Among other things if we look at the pace of growth associated with those dynamics; we don't see an awful lot of evidence of it. We're we see market based measures, like inflation expectations as proxied by TIPs, those tend to show the sort of recovery that people would refer to, but there's an alternate explanation for that that's embedded in terms of how those are calculated tips themselves have a premium associated with volatility in one form or another.

So, I'm skeptical that it does what people think it does on the MMT front, I completely agree that is growing in importance and credibility, we have not yet meaningfully seen the impact of that. The supports that we've seen in terms of a variant of universal basic income for those who are on unemployment was a very brief and fleeting experience that we've seen for give or take four months in the United States and in some other geographies to a lesser measure. But we're a long way away from a world in which everybody is receiving a significant guaranteed income from the government and the government has almost no considerations for how that actually plays through. So, if that MMT world were actually in place, I would expect that we would have seen a much more aggressive expansion of corporate profits of household incomes, etc., and the evidence is weak at this stage that's in play.

Erik: Going back to your comment about quantitative easing, not feeding through to the real economy only affecting asset markets, proponents of MMT would say that was the injustice of bailing out Wall Street at the expense of Main Street. And the whole idea of MMT is it's going to use balance sheet expansion of the central bank in order to deliver real benefits and results to the broader actual real economy. Skeptics of MMT have said, yeah, that's true, but it's going to result in runaway inflation because as you're delivering money into the real economy not just into the financial economy, now, you're going to start to experience runaway consumer price inflation. Are those arguments, right? And what are the potential consequences for markets as MMT gains traction as I expect it will, in political circles.

Mike: So, I share your view that MMT ultimately will gain increased traction. And I do think that that is likely to be an inflationary force. In its simplest form, we can think about price behavior, which is what we're trying to measure in inflation, inflation being technically an increase in the general price level, right? We can think about that as having two separate sources. One is the type of support that you're describing, which is effectively consumption subsidy, alright, so a fiscal transfer to households without significant strings or expectations of a clawback in the form of increased taxes, that is going to lead to an increase in consumption and so on net that is going to shift outward and aggregate demand curve.

It is unclear how the supply will respond and that ultimately is what kind of holds the key to this if we start to move in a pattern that restricts supply on a systematic basis that would include things like increases in corporate taxes, increases in interest rates, a reduction in the ability to execute global free trade or subsidized trade from foreign countries in the case of China. If we are unwilling to allow those sources of supply to rise to meet the increase in demand, then sure you'll see an increase in the general price level. If that increase in the general price level is in turn met by additional consumption support, additional subsidies, an increase in the minimum universal basic income that is distributed to households, then yes, you can set off an inflationary cycle.

But that's several steps into the future, we're not there yet and if anything most of the behavior that we're seeing particularly coming out of the Coronavirus experience has been that households have taken that additional income and used it to purchase things like durable goods, new houses, new cars, or used cars are in high demand because of the reduction of supply, appliances of various types, leisure craft, those have exploded and those are one time purchases, right, you're not going to buy a second RV next year if you bought one this year. You may increase some aspects of it but actually, ironically, you're less likely to stay at a hotel next year because you now have an RV, you are less likely to do many of the activities on the services front that you might have done historically, when you take a vacation you're less likely to travel in an airplane, for example.

So, it’s not at all clear that we have created a permanent outward shift in demand that there has largely been to this point as a significant substitution of durable goods for services. We’re not going back to the restaurant anytime soon, I’m certainly not going to eat two steak dinners next year to compensate for the one I missed this year. So, we’ve seen a component of that but it’s not at all clear to me that that’s sustainable, and if anything, it may set the stage for recessionary conditions in 2021.

Erik: A lot of people are debating the question of whether we are on the precipice of a shift that might take a few years but a shift to secular inflation and then perhaps MMT would be the catalyst that would get us there after this 35-year bond bull market? Now some people are saying, okay, we got all the way to almost zero it’s time for that to reverse. But frankly, people have been saying that for 15 years, and so far, they’ve been wrong. How do you see this, is the bond bull market coming to an end? Is there a secular shift to inflation? And are those things necessarily even correlated?

Mike: So, they tend to be correlated to the extent the policymakers respond to them. So, if the Fed responds to an increase in inflation by hiking interest rates to try to stop that inflation then obviously you will generate correlation, although the causation will be reversed. That was largely the story - I can flip the story of the bond bull market for the past 40 years on its head, and obviously not quite 40 years, but I can flip it on its head and say the reverse of that is that we had inappropriately tight monetary policy over the time period from 1965 to 1982 and instead of thinking about it from the framework of we have had this extraordinary recovery. I would actually suggest that we had an extended time period in which monetary policy ran way too tight relative to the expansion of the labor force and the population and the desire for consumption of durable goods under that setting.

So people tend to confuse the story of the 1970s, they think of it as a hyper inflationary type environment that the US was losing control, What was really happening in the 1970s was that we had an unprecedented expansion of households and labor force all of which needed new durable goods to meet their consumption objectives. The Fed misinterpreted that information hiked interest rates to levels that they never should have been hiked to and in response created the conditions of the resurgence that we've seen over the past give or take 35 or 40 years.

Erik: Mike, I want to pick up on the word hyperinflation that you just used because I noticed a resurgence in popularity of this term. And particularly a phrase you just alluded to, you'll hear people say, look, we're going to have hyperinflation, just like the hyperinflation we had in the 1970s. Now to my understanding of the textbook definition of that phrase hyperinflation, what happened in the 1970s has nothing to do with hyperinflation. Please define exactly what does hyperinflation mean, was the 1970s event, or other similar periods of inflation running up into the teens on an annual basis, is that hyperinflation or is hyperinflation, something different?

Mike: Hyperinflation is something totally different. So, I'm going to get the technical definition wrong because it's somewhat irrelevant, but the technical definition of hyperinflation somewhere in the neighborhood of 15% inflation per month, not per year and so by an order of magnitude, we never came close to achieving hyperinflation in the United States.

What we saw in the 1970s was a fantastic shift outward in the aggregate demand function tied to the baby boomers, tied to women entering the labor force, tied to minorities entering the labor force and the simultaneous restriction of supply that was created by the feds inappropriately tight monetary policy. So they effectively prevented the supply curve from shifting outwards and we had the really unfortunate dynamic associated with oil shocks, etc., that took roughly a third of the production capacity in the US combination of the less unfortunate Clean Air Act, and the oil shocks of the 1970s that had the unfortunate impact of shifting inward the US production curve, about a third of production going into the 1970s was tied to oil fired generators.

That dynamic is just radically different than the collapse of a currency and the collapse of a social system effectively the ability to tax to recover currency that occurs in hyperinflationary environments. People tend to completely conflate the two, I agree with your push back, we did not have hyperinflation, I think it would be extraordinarily unlikely that we have hyperinflation in the United States, although we certainly could have higher levels of inflation for the reasons we've been talking about but the underlying characteristic is just a radically different environment.

Erik: I think this is really important for listeners to understand because a trend that I'm seeing is people for good reason think that there is a macro argument that we may be headed for a secular shift back toward inflation from disinflation, I think they're right about that. What they're doing is they're going and researching the Weimar hyperinflation and various other hyperinflations like Zimbabwe that have happened throughout history, and I would argue a hyperinflation like Weimar or Zimbabwe is a completely different phenomenon from secular high inflation like we had in the 1970s. It's the collapse of a currency system, prices are not going up, the value of money is collapsing, and it creates the illusion of prices going up.

But I think what's missing here is there's really no sane reason to think that the US Dollar, at least while it still holds its title as global reserve currency. That's something I want to come back to a little bit later on. But as long as it's still the global reserve currency, I don't think true hyperinflation is even possible, but a return to secular inflation along the lines of what we really did have in the 1970s, seems entirely possible, especially in the wake of MMT. So, what if we shouldn't be trying to compare this to Weimar Germany or Zimbabwe? What is it that investors should really be looking at? What do we need to get up to speed on here?

Mike: Well, I would suggest that you actually want to look at time periods where we have had inflation driven by the forces that you're talking about. And so a good example of that would actually be the US environment post the Roosevelt depreciation of the dollar that you know Luke Gromen and others talk about that dynamic. I think it's important to understand that you can't actually have that type of depreciation, you can't have a devaluation of a currency that has a flexible exchange that happens in the markets, and so you would have to see that currency fall significantly versus other currencies, including gold, that would be one example.

But it's very difficult to actually execute that in a system in which you have a floating system because the market would do that for you before you decided to do it, it would recognize that this dynamic existed. If you look at the 1930s, basically after give or take 1934, we tend to think about that period as one that has deflationary characteristics. But actually average CPI inflation over that time period was north of 4% and it was driven by precisely the features that we're talking about restriction of supply, the forcing of crops to be fallow, the crop lands to be fallow the FDR administration paying people to not plant restrictions on production in terms of what was allowed to be produced in factories, those types of dynamics lead to inflationary conditions.

But that type of moderate inflation is both largely benign and highly unlikely to show up in a bond market in terms of a Federal Reserve policy response. And two, I think largely people misunderstand the dynamics or the importance of that because it's that type of inflation, by and large is just a modest loss of purchasing power, it's not a collapse of the currency, it's not an impetus to rush off into alternative currencies or to try to protect your assets. I think you need to be just very cognizant that we could enter into a regime that because of restrictions of supply, reduced supply from China or other regions, that we could have inflationary conditions.

Now, some of those conditions are also very difficult to point to and say they're equivalent, right? So global population was growing rapidly over that time period over the time period of the 1930s, the US labor force and population grew by roughly 25%. We just don't have those conditions in the developed world, if anything, we're actually seeing negative population pressures and most regimes, and that tends to result in an inward shift of aggregate demand. That would be even worse for talking about a situation where aggregate supply is restricted and therefore purchasing power or surplus is reduced. So, I think you could actually end up with a low inflation, but very stagnant type environment for an extended period of time if that's the outcome. And that tends to lead to increased political pressure for even more MMT and conflict for finding somebody else to blame and I do think that there are features of that that exist.

Erik: Now what a lot of people are predicting is that if that type of inflation resurfaces and there is still an impetus for the government to try to maintain the lowest interest rates that it possibly can, which seems to be the policy directive for now. That leads to negative real rates that has to be good for gold, gold bugs are jumping for joy expecting $10,000 gold prices by the end of next year or maybe that's an exaggeration, but certainly by the end of the decade, a lot of people think we're going to be somewhere between $5,000 and $10,000 an ounce gold because of these policies and this potential inflation shift that they see on the horizon. Is that same thinking, is that the right way to think about this? Are they missing something?

Mike: Well, I think it's certainly possible. I mean, for gold to go to give or take $5,000 within a decade would really only be a rate of appreciation somewhere in the neighborhood of 7%. Is that impossible? No. Is it a probable outcome? It really depends. I mean, one of the things that we wrote about in March was the dynamics of policy response and we're seeing that play out in real time. Where increasingly policymakers turn to risk markets and say what is the expectations channel tell us about forward economic activity.

In March, it was very clear that we were facing the worst recession in history, we had the biggest stock market, the most rapid stock market collapse outside of what we saw in the market event of 1987 and we've since then we've seen the most rapid recovery. And as a result, we're seeing policymakers dither in terms of their response function. Do we need another significant correction to get them to take that next step? I would suggest that it's much harder for policymakers to behave in a radical fashion unless we receive those types of signals and so I would just broadly suggest that the answer is it depends.

If events conspire to force a very aggressive response, then yes, gold will probably appreciate quite significantly, will it go to 10,000? And would we expect the behavior that we're seeing in terms of multiple expansion? Would that be consistent with gold going to 10,000? Actually, it's one of the things that we're doing some work on right now, history would suggest the opposite is true, that if gold is going to go to 10,000 that actually an equity risk premium or the P/Es, you would expect to contract dramatically because you don't pay a lot for property rights, which is really what you're doing when you buy an equity. You don't pay a lot for that in an unstable system, it's part of the reason why emerging markets tend to trade at a discount despite what many of you is better growth opportunities. The stability of the system is not such that you can look at an equity and say, I'm gonna pay 10 years worth of revenue or 100 times earnings for a company. It just doesn't make any sense.

Erik: Mike, something I've been thinking about for more than a decade is whether the US Dollars days are numbered as the world's global reserve currency and it seems like that topic has gained a lot of popularity lately. Seems to me like what this really comes down to is the US Dollar remains the world's global reserve currency for one reason and one reason only, which is there simply is no viable alternative today seems to me like a lot of people around the world have increasing impotence or motivation to try and find one. Would you agree with that? And if so, what do you think the greatest threats are in terms of what other nations might do to look for an alternative to the Dollar?

Mike: So, I think your observation that there is no alternative is probably the right one and there are always risks to the replacement of the reserve currency. But again, it tends to be the function of a violent shift and so the transition from the British Pound to the US Dollar was a result of the aftermath of World War One where the British were forced to borrow in large size from the Americans and ultimately, that meant that the supply of Pounds to the global regime was far greater than could be maintained.

And simultaneously, the UK tried to move back to the gold standard levels which created inappropriately tight monetary policy, etc. That type of transition of course can occur if there's an event of that type of magnitude that changes the US status in the world but that's hard to achieve. I mean, it would require a legitimate repudiation of the dynamics of the Pax Americana where it became clear that the US was no longer able to enforce property rights or claims in regions around the world. We still are a long way away from that, while there are potential rivals in the form of a unified Europe, which took its strongest form and under the Euro has created its own challenges.

Also, you have to consider China as a somewhat legitimate threat to that dynamic, they're just far from clear replacements. And if anything, while people talk about the loss of reserve currency status, the US share of global trade when properly measured by looking across regions, not necessarily states has continued to rise, it's become more dominant, not less dominant. Now, in terms of the incentive structure that you refer to the US has also become much more aggressive in terms of using or weaponizing the Dollar, and that does create incentives for people to respond. But it's very difficult to openly mount a challenge to the global hegemon, it would require an overt act that would have significantly negative impacts on most of the countries that are talking about this, which by and large are running current account surpluses which means that they are beholden to the US to buy their goods and services. That's just it's gonna be really, really hard to replace that.

Erik: Mike, here's my contention on how that might be replaced and I wrote a book about this a couple of years ago, I think that the invention of the secure digital bearer asset, which was invented by the Bitcoin crowd several years ago is a game changer. I think it's going to completely change the course of human history.

Now, I don't mean that I think Bitcoin is going to replace the Dollar in any capacity. What I do mean is that the underlying technology a digital bearer asset which can securely operate in a decentralized global network and truly act as a bearer asset, I think that provides the foundation for the creation of a digital currency system. With the opposite objectives of Bitcoin; Bitcoin was designed to defeat monetary policy to essentially resist the existence of the fractional reserve banking system. I anticipate that Silicon Valley will eventually invent a digital currency system designed to be sold to central bankers, one that delivers radically enhanced monetary policy capabilities whereas Bitcoin was designed to defeat monetary policy, something that is designed to be sold to central bankers as a superior alternative to the US Dollar.

And although that unto itself is a pretty compelling sales pitch to replace the US Dollar but it's hard to replace something that's as entrenched as the Dollar is look at the number of countries around the world that are so frustrated by the weaponization of the Dollar that you just described. And I think that provides the adoption catalyst needed to adopt that digital currency, if that were to happen and suddenly the US government didn't have its position of hegemonic control over the financial system. I think things could get ugly, it could easily start a war, but I don't think that that war would necessarily prevent the new currency system from taking over. Those are obviously some pretty extreme out their views, I'm very curious to get your perspective. Am I crazy to think these things?

Mike: I don't think you're crazy to think these things I think that like most futurist views it's somewhat perpetually 10 to 20 years off into the future and by the time we get there we realize it was 100 years off into the future. The challenge with that view is I would say twofold. One is it doesn't matter how many countries are upset about stuff and so like children on the playground they can be upset about the school bully, but until one of them hits puberty and can legitimately challenge him, it doesn't really matter. He's still going to take your lunch money and the US has been by and large quite benign in its behavior relative to prior global hegemonic.

I frequently cite the dynamics of the Roman Republic and its transition to the Roman Empire, one of the best examples of that type of dynamic is one of the kings of a neighboring kingdom, donated quote unquote, his country upon his death to the Romans. And you look at this Like why in the world would you give the country to the Romans? The reality is you gave it because otherwise they're going to take it and you are hoping to secure a better and more favorable terms. I think by and large the world has taken for granted that the US is going to behave in a benign fashion if those types of challenges occur and the US is somewhat uniquely positioned globally as controlling its own island.

If you think about it from the dynamics of a castle, we've got the world's best moats on the east and the west, we have a somewhat incompetent barrier to entry to the south and we've got a frozen tundra to the north with its denizens huddled around our village gates. If we decide that we're going to get serious about exploiting our position as the global hegemon I don't think there's a chance that the rest of the world is prepared for that at least yet. If they decide to build their own militaries, if they decide to finance those components, if they decide that they're going to risk their women and children, then sure that can happen, but I think it's a long way away.

Erik: And if I correctly understand, this is about military dominance and certainly history teaches us that the global reserve currency status has gone to the country with the strongest military. Doesn't the emergence of hypersonic carrier killer missiles from China and some of the other military developments that suggest the US no longer is an undefeatable force of power in the world? Does that change the game? Or do you really need to get to the point where the US is not only undefeatable, but it's actually been defeated in some capacity before the currency can change?

Mike: Yeah, I would lean towards that dynamic and I would suggest that while those are certainly impressive military technology, as were German V2 rockets and the dynamics of blitzkrieg we'll eventually figure out solutions to them. The US tends not to go out and broadcast what it is capable of doing. I would be surprised that the local bully reveals all of his, at least if he's a smart player, reveals all of his capabilities. It's much more likely that there's a fake challenger that's trying to point to their strengths in the hope that they will get others to follow.

Erik: Mike, you're describing military might as the key determinant here. Are you expecting a military conflict? Obviously, we have big escalation of tension between the US and China and so forth. Do you think that a shooting war between the US and another sovereign nation is on the horizon? And if so, who are the potential combatants and what does it look like and what does it mean for the world?

Mike: So I actually hope that we don't have that and I would say to expect that would be somewhat foolish right? My biggest fear as I describe the dynamics that I refer to is that the US in appropriately responds and more aggressively responds to defend these dynamics that I've described to them they have to write the biggest risk that we have as the United States is that we cease being what we have historically represented a beacon of "freedom", right? And you can debate that all you want but the US has historically been one of the primary destinations for those who are choosing to leave unfavorable conditions and the hope of a better life, right. There's a very real chance that we break that system as we're moving to defend what we perceive to be our strengths, I hope that's not the case.

Erik: Mike, before we close, I want to shift gears here and talk about some of the work that you're doing at Logica. I think that you're just an absolutely brilliant thinker and you've got a lot of terrific perspective on markets and where they're headed. You used to be kind of locked away behind a compliance wall and couldn't talk to anybody these days. At Logica you've got the freedom to do some writing, so please tell our listeners what you do at Logica, certainly we do have a very large accredited investor base who may be interested in some of your investment offerings, but for everyone else, I think there are some very interesting white papers and other resources available at LogicaFunds.com please tell us about that as well.

Mike: So we use our website to provide access to our research and our white papers we've written on the dynamics of policy and the time of pandemics we've written about the value growth or value momentum debate that's currently in play. We recently put out a piece talking about the dynamics of the options skew the call option skew this caught a lot of attention and explained that largely in the form of reduced supply combined with the aspects of demand that has been well telegraphed. Then we're about to put a piece out talking about the dynamics of the gold market, and so I would encourage people to check that out from a product standpoint, our flagship product is the Logica absolute return product, it is only available to accredited investors and institutions. We do partner with a couple of other groups to provide access to our vehicles and so people are more than welcome to register and reach out in terms of that information, we encourage them to do so.

Erik: Well, Mike, I can't thank you enough. For a terrific interview Patrick Ceresna and I will be back as MacroVoices continues right after this message from our sponsor.